

## **Korn Ferry (KFY)**

### ***The Executive Suite Goes Digital***

*“I’ve heard a lot about Korn Ferry’s ability to build a brand around digital transformation and attract the right leaders...and to make use of the data and insights to drive strategic sales growth...as we prioritize our own digital transformation, they’re favored to win projects” – HR executive from a \$10bn+ global business*

With premium assets trading near multi-decade highs, the market has overlooked one hiding in plain sight. We’re long Korn Ferry (KFY), the world’s most illustrious executive recruiting firm. Long typecast as a deep-cyclical and priced at 11x F2021 P/E and 7x EV/EBITDA, recent disclosures reveal a pair of cyclically resilient business units with above-industry growth. This quarter, KFY will begin reporting a “KF Digital” segment that consolidates its world-leading compensation databases, leadership development platforms, and sales training modules into one reporting disclosure. These products remain at the client under license well after a recruiting or consulting assignment concludes, creating a durable revenue stream with high incremental margins. By the next fiscal year (beginning April 2020), KF Digital should generate \$400m of revenue and over \$100m of EBITDA (27-30% margin target), or about one third of the company’s consolidated EBITDA.

At the same time, Korn Ferry has quietly built a leading recruitment process outsourcing division (“RPO”) boasting 19% compounded growth over the past five years and 20% and 27% growth over the prior two quarters. Customers speak highly of the RPO’s technology platform, implementing its AI sourcing tools to improve the hiring efficiency and cost for skill-based roles. By leveraging its global footprint and sourcing platforms, the RPO can handle thousands of assignments at \$1-3k per hire versus 20-30% of salary in the traditional model, positioning itself for years of share gains over traditional staffing firms. In the most recent quarter, KFY signed \$118m of longer-term RPO contracts, up from \$41m last year; the RPO business is booming.

Yet Korn Ferry receives little credit for these prized assets, with a forward P/E multiple of 11x and an unlevered free cash flow yield near 7%. These valuations, a byproduct of comparing KFY to sub-scale search firms like Heidrick & Struggles (HSII) and temp agencies like Robert Half (RHI), are utterly incongruous with Korn Ferry’s newly disclosed business mix. By the end of calendar 2020, KF Digital should reach \$110m of EBITDA while Korn Ferry’s pure-RPO operations (excluding professional search revenue) could annualize \$45m of EBITDA, amounting to over 40% of Korn Ferry’s total EBITDA. Premium valuations abound for comparable assets: Huron Consulting (HURN), a healthcare and education consultant group, trades for over 15x 2020E EBITDA; FTI Consulting (FCN), a corporate restructuring and legal consulting company, trades for 13x 2020E EBITDA; and Learning Technologies Group (LTG), a recruiting, compliance and training software firm with 30% EBITDA margins trades in London at 22x C2020 EBITDA. As for the RPO business, billion-dollar private equity deals for Alexander Mann and Cielo were recently completed at EV/EBITDA valuations well above KFY’s modest 7x EV/EBITDA: investment bankers at SunTrust place the average RPO transaction at 14x

EV/EBITDA since 2015. At just 12x EV/EBITDA for Digital and 14x for the pure-RPO – fitting for KF Digital's higher margins in KF Digital and embedded growth in RPO – the combined \$2.0bn valuation covers KFY's current enterprise value almost on its own.

That leaves almost \$200m of EBITDA in KFY's Executive Search and Consulting segments unaccounted for. KFY's Executive Search business still has the prestige of a McKinsey or Goldman Sachs for C-suite and board recruitment. And the Consulting practice can contribute consistent multi-year growth even through periods of global uncertainty. With recent business surveys and forward indicators pointing to executive hiring intentions bottoming off recent troughs, KFY's Search and Advisory should recover in the coming quarters. Even using the Street's no-growth projections for the Executive Search and Advisory businesses through F2021 (beginning April 2020), KFY should produce \$175-200m of annual free cash flow with a clean balance sheet (the upcoming FQ3 and FQ4 are seasonally the most cash-generative quarters). And while Search and Advisory will show some economic sensitivity over a quarter or two, we've witnessed these businesses grow through economic slowdowns in 2011, 2013, and 2016.

The company's clean balance sheet and cash-generative core business will allow Korn Ferry to invest further into its Digital businesses. On November 1, KFY closed on a trio of acquisitions for the Digital portfolio that add \$0.40-\$0.45 of run-rate EPS and \$35-40m of EBITDA to the consolidated business in F2021. We'd expect KFY to build on its acquisitions of Miller Heiman, AchieveForum, and Strategy Execution to add additional digital assets once synergies and cross-selling opportunities are fully realized on the November deals. With these investments, KFY's business transformation into a digital-first, RPO-driven business should accelerate into next year.

Public markets may see the first pure-play RPO in the next year or two as private equity looks to monetize their Alexander Mann and Cielo investments. A fresh set of public comparables would help uncouple Korn Ferry's valuation from temp staffing firms like Robert Half (RHI) and search boutiques like Heidrick & Struggles (HSII). Using our estimates for the RPO and KF Digital units and a 7-8x EV/EBITDA multiple on Search and Advisory units – in-line with current comps and KFY's 10-year average – we project a target price of \$60-65, more than 50% higher than current trading levels. If Search growth returns in earnest, we think KFY can trade up to \$80, a valuation supported by its robust cash flows. It's time to reap the benefits of this digital transformation and ferry capital into KFY.

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## I. Investment Highlights

Capitalization	
	FQ2A
<b>Share Price as of 02/03/20</b>	<b>42.17</b>
Diluted Shares	55
<b>Market Capitalization</b>	<b>2,307</b>
Plus: Total Debt	273
Add: Cash for Deferred Comp	263
Add: Cash for Recent M&A	113
Less: Cash and equivalents	(609)
<b>Enterprise Value</b>	<b>2,347</b>
Operating Leases	249
Lease Adjusted EV	2,596

KFY Trading Statistics <sup>(1)</sup>			
	FY 12/31		
	F2019A	F2020E	F2021E
EV / Revenue	1.2x	1.2x	1.1x
EV / Adj. EBITDA	7.6x	7.7x	6.9x
EV / Adj. EBIT	11.6x	9.5x	8.1x
P / E	12.6x	13.5x	11.4x
EV / FCF	14.2x	16.0x	10.1x
FCF / EV	7.0%	6.3%	9.9%

(1) Consensus estimates

Base Case Price Target				
	F2021E			
	Revenue	EBITDA	Mult	Valuation
KFY Core	\$1,931	\$193	7.0x	\$1,348
KFY RPO	252	43	14.0x	599
KFY Digital	424	121	12.0x	1,450
Less: Net Debt <sup>(2)</sup>				(40)
Implied Market Capitalization				\$3,358
<b>Implied Share Price</b>				<b>\$61.36</b>
<b>Upside</b>				<b>45.5%</b>

(2) Subtracts \$112.5m of FQ2A cash for Digital acquisitions

Bull Case Price Target				
	F2021E			
	Revenue	EBITDA	Mult	Valuation
KFY Core		\$205	8.0x	\$1,640
KFY RPO		43	14.0x	599
KFY Digital		121	12.0x	1,450
Less: Net Debt <sup>(2)</sup>				(40)
Implied Market Capitalization				\$3,649
<b>Implied Share Price</b>				<b>\$66.69</b>
<b>Upside</b>				<b>58.2%</b>

### **Newly Disclosed Financials for Korn Ferry Digital Business and M&A Accretion to Drive**

**Valuation Upside.** Two aspects set Korn Ferry apart from others in the staffing industry: a 50-year heritage with a top-tier brand name and a rich set of proprietary data and applications built through its decades of experience. By working on more assignments than others, tracking offered and accepted salaries, and developing leadership teams for its clients, Korn Ferry created digital platforms backed by hard data and stress-tested over many years. KFY now owns compensation records for 20 million people and competency profiles on 1.2 million executives, among other mineable databases. According to customers we've spoken to, products like Korn Ferry [Pay](#) (used by over 70% of the Fortune 500), Competency Profile [Manager](#), KF Interview [Architect](#), and Executive Success [Profiles](#) have become industry standards. Until now, these products were co-mingled with the Advisory business, giving investors little visibility into their size, margin profile, or growth potential.

But this changes next quarter. Korn Ferry's existing Digital business (~\$275m of revenue) will coalesce with three recent acquisitions (\$125m of revenue) to create a \$400m business with 27-30% EBITDA margins by April 2020 (the start of F2021). The digital business will offer everything from rewards databases to training and development, with exciting cross-selling potential as Korn Ferry leverages its global, blue-chip customer base. Management believes the business can grow revenue in the mid-to-high single digits with less cyclicity than executive staffing, making KF Digital more comparable to a data services business than a legacy recruiter.

The November acquisitions of Miller Heiman, AchieveForum, and Strategy Execution also offer immediate accretion to next year's financials. Since KFY can leverage existing customer

relationships without the need for additional selling or marketing costs, it expects these acquisitions (and restructuring efforts within Digital) to add \$35-40m to its run-rate EBITDA and \$0.40-\$0.45 to EPS. Markets may have overlooked this upside since current FQ3 guidance includes little near-term accretion, but that's because an expensive shared services agreement remains in place until FQ4 2020. As this contract lapses and KFY works through one-time severance costs, the upside for F2021 will become readily apparent.

### Acquisitions to Add \$35-40m of EBITDA in F2021

Revenue	F2017	F2018	F2019	LTM	GS	ProFrm
					F2020E	F2021E
Executive Search	618	709	775	765	733	770
KF Consulting	498	541	568	539	518	544
KF Digital	227	245	253	275	275	424
<i>Memo: November Acquisitions (\$125m FY, closed Nov 2019)</i>					83	
Total Advisory	724	785	821	814	876	968
Pure-RPO	--	--	175	192	210	252
Professional Services	--	--	155	171	175	193
Total RPO	224	273	330	363	385	444
<b>Fee Revenue</b>	<b>1,566</b>	<b>1,767</b>	<b>1,926</b>	<b>1,942</b>	<b>1,995</b>	<b>2,182</b>
<b>EBITDA</b>						
Executive Search	137	159	194	191	177	185
KF Consulting	--	--	--	--	67	71
KF Digital	--	--	--	--	84	121
Total Advisory	128	144	151	149	151	192
Pure-RPO	--	--	--	--	36	43
Professional Services	--	--	--	--	30	31
Total RPO	33	43	54	61	66	74
Corporate Overhead	(63)	(67)	(88)	(87)	(88)	(94)
<b>EBITDA</b>	<b>235</b>	<b>278</b>	<b>311</b>	<b>313</b>	<b>305</b>	<b>356</b>
<b>Y/Y Growth</b>					(3%)	17%

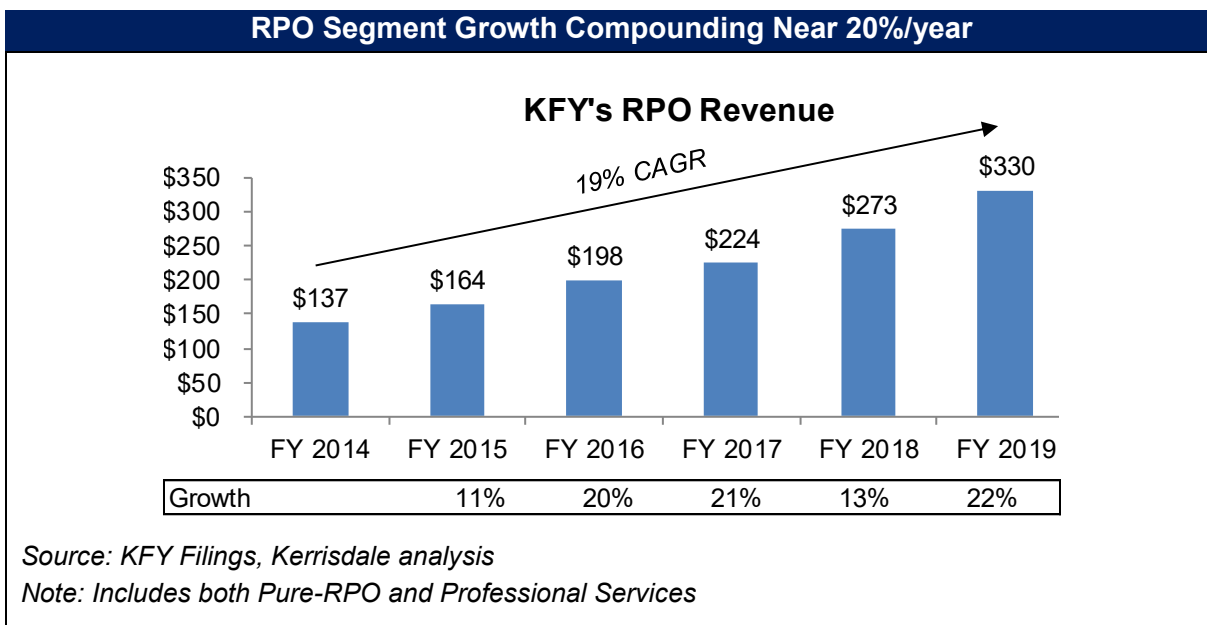
Source: KFY Filings, Goldman Sachs Research, Kerrisdale analysis

Of the \$400m in new KF Digital revenue, roughly \$100m comes from rewards databases, \$120m from talent assessment, \$120m from learning development, and \$60m from organizational strategy. While already substantial, CEO Gary Burnison sees additional assets to monetize for its Digital business over time, "So I believe that there is a substantial amount of energy in the organization around mining the data, packaging it with IP, and then trying to productize it" (FQ1 2019 Call). Organic investments like this, combined with potential additional acquisitions in F2021, mean that KF Digital will only become a larger part of the business mix over time.

**Korn Ferry's RPO is an Underfollowed High-Growth Asset.** Named a leader in both the Everest Re Global RPO [survey](#) and HRO Today [ranking](#), Korn Ferry's RPO segment has grown

from less than 10% of KFY’s EBITDA to almost 25% by the end of 2020. This success mirrors an industry-wide shift towards RPO firms, with the industry [expected](#) to grow 20-30% over the next five years. Workforce churn is a daily challenge for internal HR departments: tenured floor managers join a competitor, data scientists find higher paid work elsewhere, and engineers take their talents on the road. And in the age of LinkedIn, dozens of job boards, and ever-increasing Google SEO complexity, a single HR or talent executive can no longer manage the dozens of software systems and processes required to replace this ever-present churn in the organization.

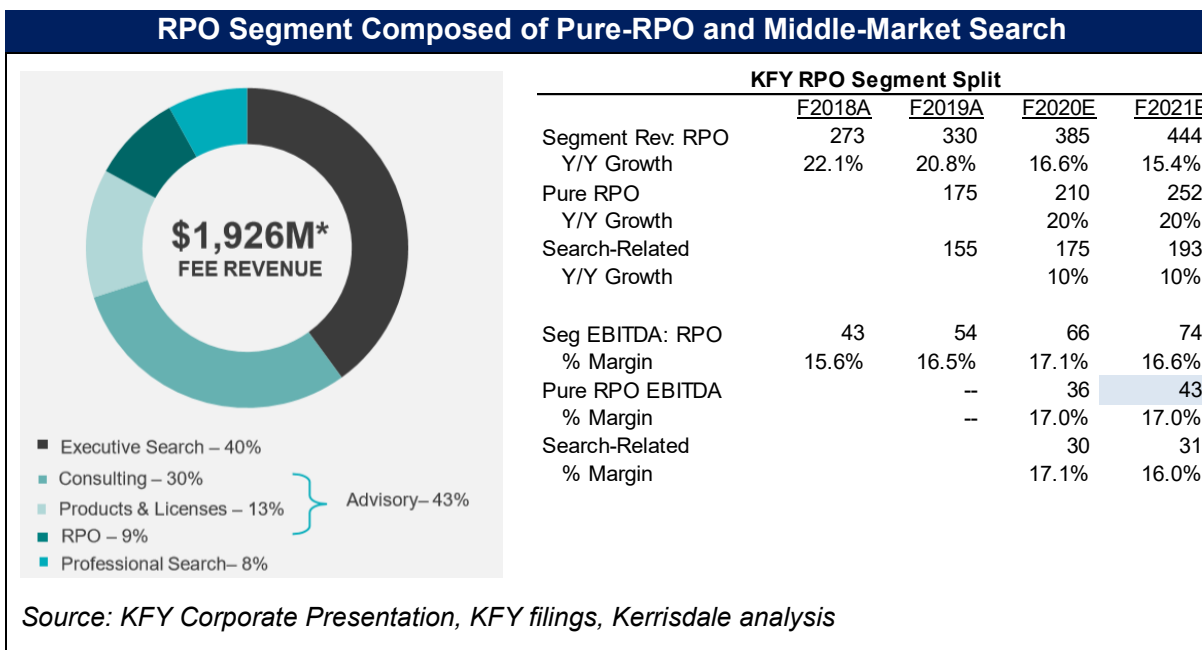
Korn Ferry’s RPO business was built over many years to address these concerns. The Futurestep brand, now retired under the Korn Ferry banner, was first [created](#) in 1998 (plans were even made to create a [tracking](#) stock before the dot-com crash). KFY’s RPO segment includes both “Pure-RPO” and Professional Services; the latter includes middle-management assignments too junior for the executive search segment. Combined, these two segments have grown at a 19% CAGR over the five years.



Pure-RPO assignments are signed with global customers for multi-year, large-scale hiring initiatives. These contracts provide greater revenue visibility than one-off assignments – the chart above is proof of that – and justify the premium valuations earned by the RPO group. We’ve therefore modeled the Pure-RPO business separately using stable growth rates and margins from the disclosed figures at F2019. Under these assumptions, we calculate almost \$45m in pure-RPO EBITDA by the end of F2021. If we added the Professional Search sub-segment, a reasonable inclusion since the services are co-mingled elsewhere and Professional Services also grows rapidly, then the RPO’s EBITDA attribution would double.

Korn Ferry’s RPO benefits from the premier brand of its parent company. In many instances, CEO or CFO hiring assignments form the relationships which eventually lead to a large RPO deal. In the most recent quarter, about 35% of the RPO’s new business originated from

Executive Search referrals. Most of the RPO competition can't match the brand recognition of Korn Ferry.



On its quarterly calls, KFY also discloses new business wins for the RPO segment. Using these metrics, the new deal pipeline appears as healthy as ever, with \$118m of new Pure-RPO business signed in FQ2 2019. Whatever Brexit and Trade War related softness was felt in Executive Search this prior quarter, it's nowhere to be seen in the RPO segment.

**Quarterly Contract Wins for RPO at Seasonal Records**

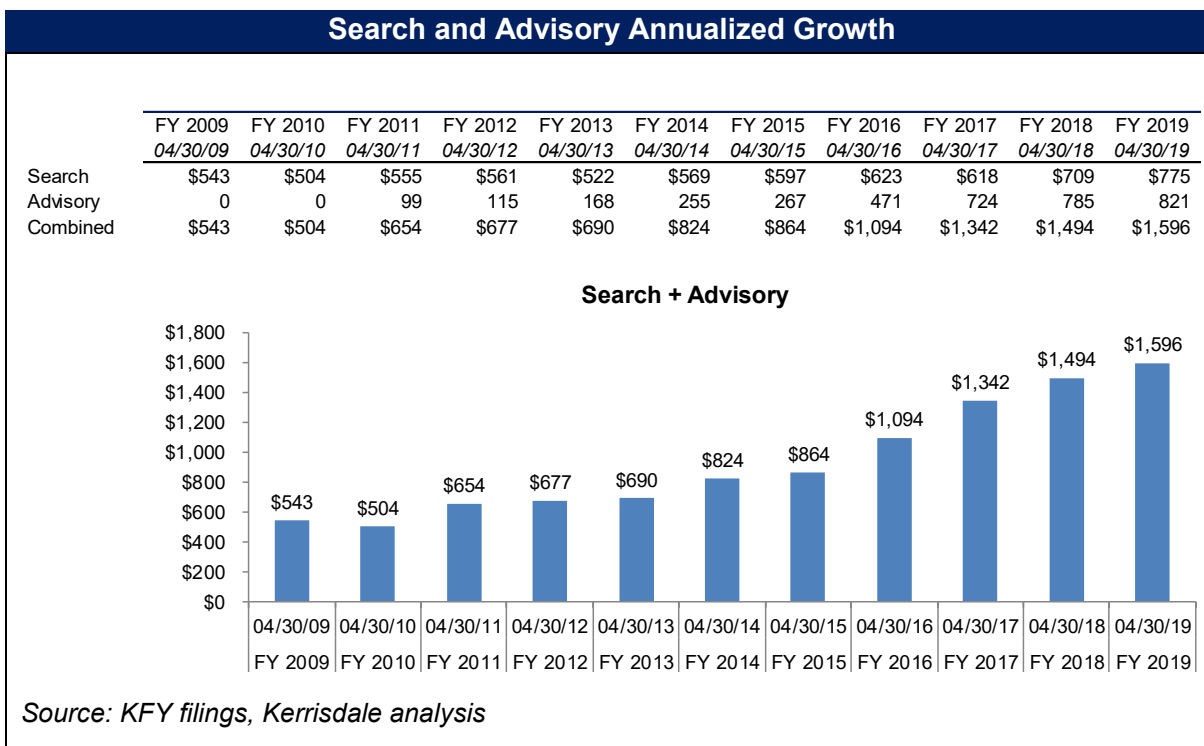
	Q4'18	Q1'19	Q2'19	Q3'19	Q4'19	Q1'20	Q2'20
	04/30/18	07/31/18	10/31/18	01/31/19	04/30/19	07/31/19	10/31/19
<b>RPO New Business</b>	<b>158</b>	<b>70</b>	<b>73</b>	<b>104</b>	<b>84</b>	<b>97</b>	<b>150</b>
Professional Search	38	31	32	26	34	31	32
<b>Long-term RPO contracts</b>	<b>120</b>	<b>39</b>	<b>41</b>	<b>78</b>	<b>50</b>	<b>66</b>	<b>118</b>
Of which: new logos				19	44	32	49
Of which: extensions				59	6	34	69

Source: KFY Quarterly Calls

With their high-quality growth characteristics, RPO valuations are deservedly rich. SunTrust Research pegs an average transaction value of 14x EV/EBITDA since 2015, "Over time, we believe that a stand-alone RPO unit (20% of '21E company sales) could fetch 15x EBITDA in today's market (the median multiple for RPO businesses has been 14x since '15)." Kerrisdale's own diligence confirms this figure, with industry participants citing a "mid-teens" multiple for recent RPO deals for Alexander Mann and Cielo, both acquired by private equity. If we

conservatively employ a 14x EBITDA for KFY's Pure-RPO segment, the business should be worth almost \$600m by the end of 2020.

**Advisory and Search Resilient Through the 2011, 2013, and 2016 Slowdowns.** KFY shares underperformed the S&P 500 by almost 30% in 2019 after Search and Advisory revenue growth slowed from 10-15% to the low-single digits (constant currency), the result of FX headwinds, difficult y/y comparisons, and weakness in Europe and Asia. While these segments remain exposed to events such as the UK election and Trade War disruption, Search and Advisory have managed to grow through comparable periods in the past. Cyclical slowdowns in 2011, 2013, and 2016 also caused Search volumes to contract over 1-3 quarters, but, when measured annually, Korn Ferry offset any hiccups with quick organic recoveries or additions to the Advisory business. The chart below demonstrates the business' resiliency and ability to grow into a vast global end-market.

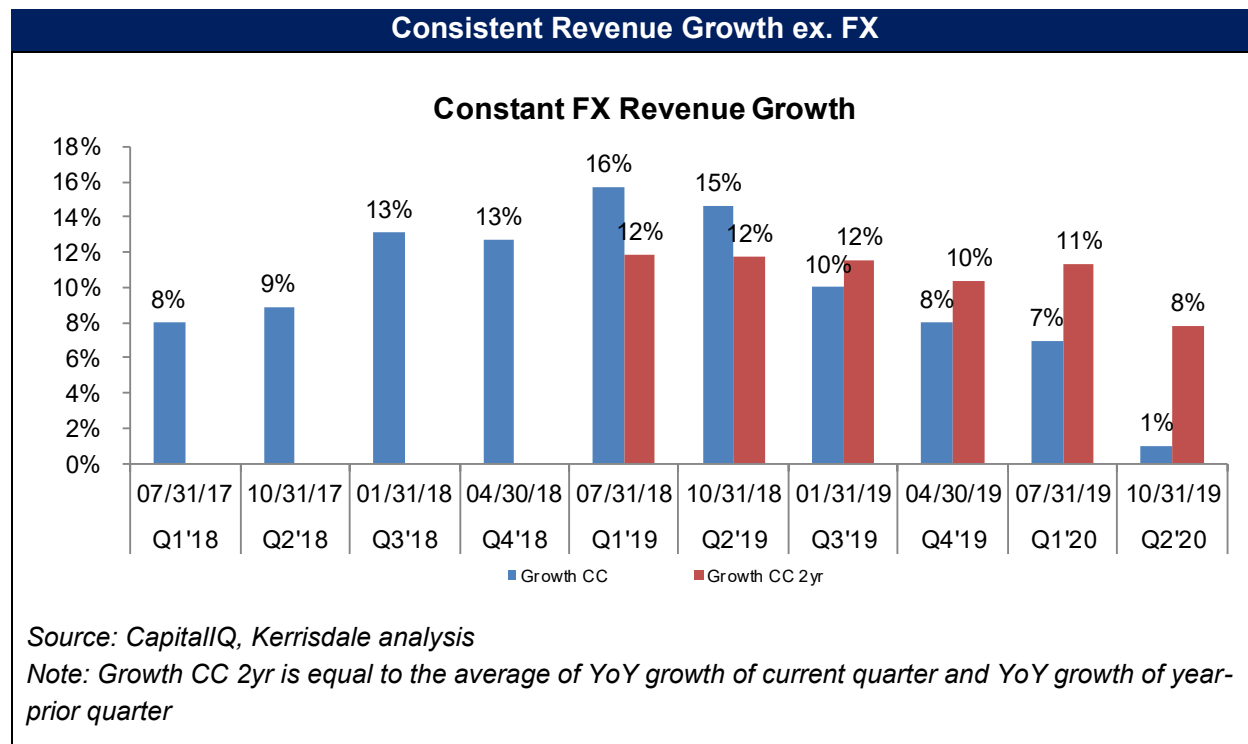


This resiliency should increase as KFY increases its proportion of “Marquee” clients, those representing global accounts who are buying services across business lines. As of the F2019 10-K, Marquee accounts represented 21% of revenue, but that figure has grown over the first two quarters. Marquee accounts grew 9% y/y constant currency in FQ1 and 6% in FQ2, both well above the Company average. As Korn Ferry works towards its target mix of 40-45% for Marquee and Regional clients, these larger enterprises should add stability to the Search and Advisory businesses.

As for the near-term, we see easier mathematical comparisons for KFY going into F2021. Although headline growth decelerated in FQ2 (+1% constant currency), and guidance projects



similar trends in FQ3 2020 – Brexit, elections, and Trade War skirmishes have impacted European search volume in November – these figures are comping against very difficult year-over-year comparisons. When measured on 2-year stack, constant currency growth still averaged 8% in FQ2 (in other words, the average of annual year-over-year growth in FQ2 2020 and FQ2 2019 is 8%). And year-over-year comparisons will ease significantly going into F2021. If prior years are any indication, Search and Advisory will soon return to 5-10% growth.



**Leading Indicators Point to Continued U.S. Search Demand and a Recovering European Staffing Market.** Challenger, Gray & Christmas, an industry thought leader, tracks domestic CEO departures on a monthly cadence: its December headline proclaims, “160 CEOs Out in December, Highest Annual, Quarterly Totals on Record.” In the fourth quarter, CEO departures reached 480, a 11% jump from the prior record of 434 set in Q3 2019. These transitions create a healthy pipeline of deals for Korn Ferry, whose Executive Search team is typically in the pole position to replace any outgoing CEO.

## Domestic CEO Departures

### CHALLENGER CEO REPORT CEO DEPARTURES By Month

Month	2019	2018	2017	2016	2015	2014	2013	2012	2011	2010	2009	2008
January	157	132	128	131	110	131	113	123	96	89	113	134
February	124	113	72	87	94	112	110	104	92	132	82	114
March	135	96	101	101	95	123	86	94	99	119	114	123
April	97	109	91	108	97	94	94	90	103	101	78	112
May	114	91	80	100	90	98	104	99	103	125	115	115
June	99	90	95	97	102	103	94	99	113	107	105	126
July	124	94	102	92	128	105	128	83	104	88	126	124
August	159	154	96	109	107	119	113	104	104	95	101	144
September	151	148	101	119	104	124	107	95	108	111	105	140
October	172	149	105	99	94	122	104	108	91	81	89	125
November	148	147	94	106	86	103	94	112	82	79	94	104
December	160	129	95	99	114	107	99	103	83	107	105	123
<b>TOTAL</b>	<b>1,640</b>	<b>1,452</b>	<b>1,160</b>	<b>1,248</b>	<b>1,221</b>	<b>1,341</b>	<b>1,246</b>	<b>1,214</b>	<b>1,178</b>	<b>1,234</b>	<b>1,227</b>	<b>1,484</b>

Source: Challenger, Gray & Christmas December [report](#)

While the industrial economy has slowed following months of trade war rhetoric and recent disruptions in China – consistent with KFY’s FQ3 2020 guidance and lowered analyst expectations – recent employment statistics point to resiliency in the domestic jobs market. The NFIB’s small business optimism index [surged](#) in November to its largest month-over-month gains since May 2018. December hiring expectations improved month-over-month in SunTrust’s search volume survey. And most recently, the January ADP jobs [report](#) beat expectations with 213k jobs added vs. consensus of 181k at 3.5% unemployment ([December](#) BLS). With some analysts modeling KFY Search to decline 12% in FQ3 and 5% in FQ4, the market expects very little from the Search business. But if the domestic economy continues to add jobs at its current rate, KFY’s North American Search business should return to growth in F2021, reminding investors why they paid over 20x P/E for KFY shares just eighteen months ago.

## Hiring and Optimism Surveys Point to Continued Search Growth

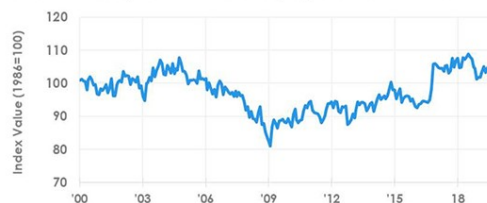
Figure 7: Expected Search Revenue & Volume Growth for Next 12 Months (Jan. 2019 – Dec. 2019)

Date	STRH POLL 12-Month Expected Growth in Revenue	STRH POLL 12-Month Expected Growth in Searches
Jan-19	6.6%	6.6%
Feb-19	9.6%	8.6%
Mar-19	9.4%	7.7%
Apr-19	6.4%	7.4%
May-19	6.0%	7.5%
Jun-19	4.4%	4.4%
Jul-19	3.8%	3.8%
Aug-19	6.0%	7.0%
Sep-19	3.5%	3.2%
Oct-19	4.5%	3.3%
Nov-19	1.0%	0.3%
Dec-19	1.4%	0.5%
<b>Trailing 12-Month Average</b>	<b>5.2%</b>	<b>5.0%</b>

Source: SunTrust Robinson Humphrey poll of private companies

### Small Business Optimism Index at 104.7

Based on 10 survey indicators, seasonally adjusted, Jan. '00 – Nov. '19



NFIB

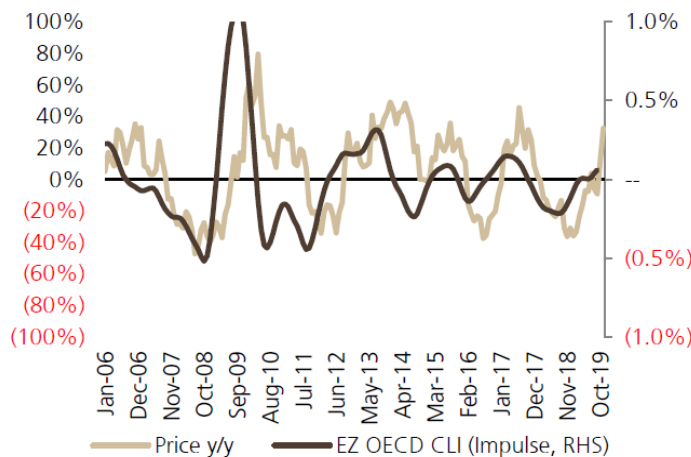
NFIB.com/sboi

Source: SunTrust Research, NFIB survey

Meanwhile in Europe, staffing trends are beginning to stabilize. The second derivative of the OECD's Composite Leading Indicators ("CLI") began edging higher in late Q3 2019. While trade war rhetoric and snap elections in the UK caused some pause amongst business leaders in the fourth quarter, recent progress on both fronts should support KFY into F2021.

## European Leading Indicators Beginning to Stabilize

Figure 14: An improving second derivative has historically lead a recovery in share prices (Adecco share price)

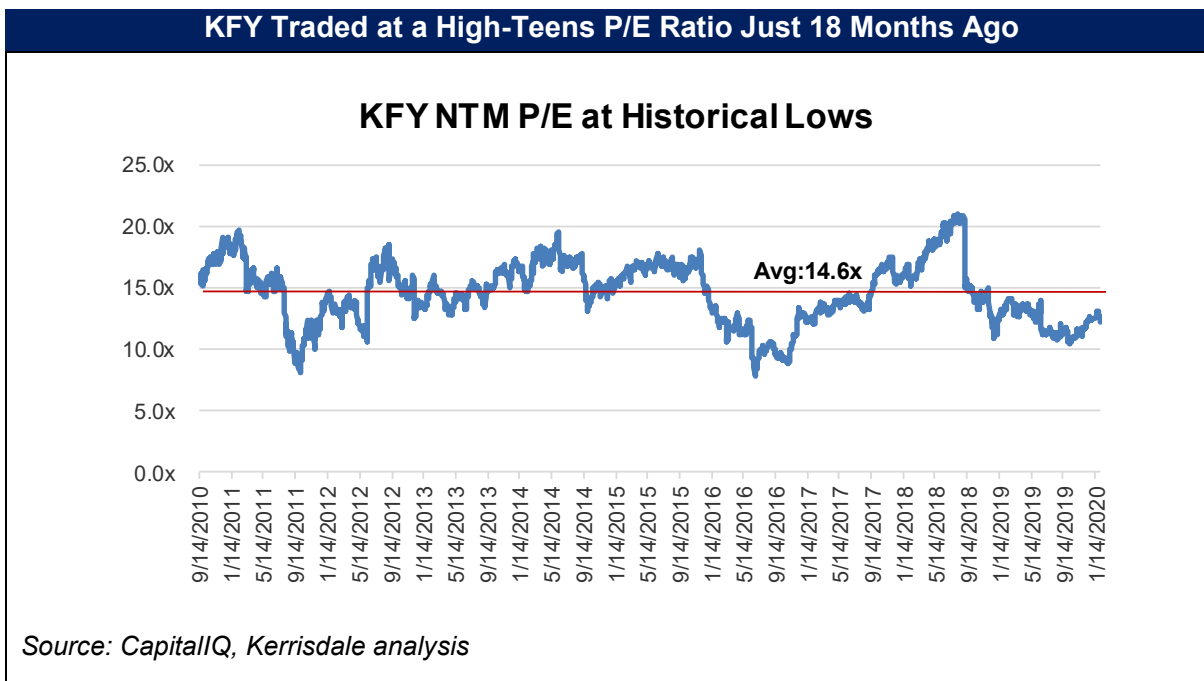


Source: Datastream and company reports

Source: UBS Research

**KFY Shares are Exceptionally Cheap Against a Seasonal Trough in FCF.** KFY shares have been under pressure during the prior few quarters, with KFY Search growth slowing from its double-digit performance in F2018. A slower industrial backdrop evoked flashbacks to the cyclical contractions of 2011, 2013, and 2016 – all excellent opportunities to acquire KFY shares in hindsight – and the market hurriedly placed recessionary multiples of 7x EV/EBITDA and 11x

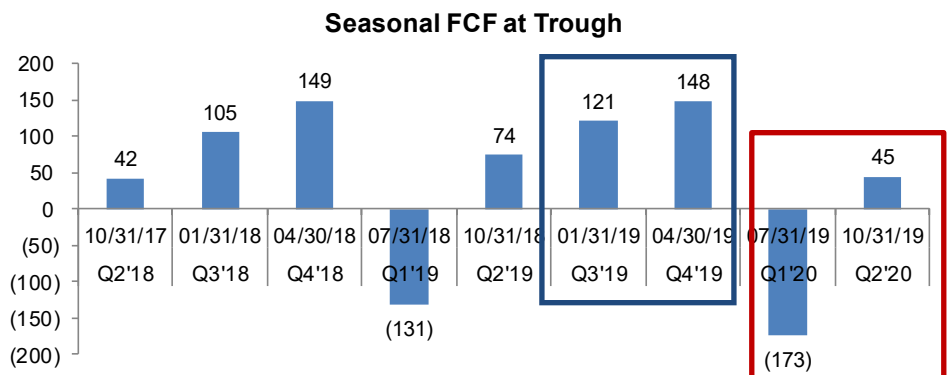
P/E on KFY’s business. Even with a recent waning of trade tensions, the U.K. election, and a U.S. stock market still grasping at highs, KFY’s P/E hovers near its historical low.



Current enterprise value calculations also underestimate Korn Ferry’s value since FQ1 includes a large cash draw for employee bonus payments. Deferred bonuses accrued throughout the year – the rewards for successful deal closings and search assignments – are paid out in FQ1, creating a once-a-year cash outflow. This seasonal outflow depresses KFY’s balance sheet and EV/EBITDA calculation until large cash inflows are received in FQ3 and FQ4. While next quarter’s FCF will be absorbed by the \$112.5m payment for the November Digital acquisitions, second half cash flow can typically add \$250m to KFY’s balance sheet, or over 10% of the current market capitalization.

**Seasonal Trough in Free Cash Flow Depresses Cash Balances**

	Q2'18	Q3'18	Q4'18	Q1'19	Q2'19	Q3'19	Q4'19	Q1'20	Q2'20
	10/31/17	01/31/18	04/30/18	07/31/18	10/31/18	01/31/19	04/30/19	07/31/19	10/31/19
Δ in NWC	1	79	106	(179)	11	74	100	(225)	(9)
CFO	53	116	160	(117)	85	133	158	(162)	58
CFO - Capex	42	105	149	(131)	74	121	148	(173)	45



Source: Company filings, Kerrisdale analysis

To maintain conservatism in our estimates, we've still based our valuation on the current depressed balance sheet and deducted \$112.5m of cash for the Digital acquisition expense (closed November 1<sup>st</sup>) – even though KFY should be \$250m richer by the end of April. This conservative tact is paired with comparable company multiples for each of KFY's business units, matching the approach we think the market will employ as KFY's Digital and RPO assets come to light in 2020. At our base case of 7x EV/EBITDA for the Search and Advisory businesses – these assets trade much higher during periods of reflation and global expansion – 12x for the Digital portfolio (in-line with digital consulting firms like FCN and HURN), and 14x for the contracted RPO business (supported by precedent company valuations and its 20%+ revenue growth history), we believe KFY can trade to \$60-65, or 50% higher than the current price. If the recruiting market improves in 2020 and the economy continues its expansion, we think Search and Consulting can outperform expectations to generate almost \$370m of total EBITDA. With a higher multiple on the core business, shares could approach \$70 vs. a price near \$42 today.

Price Target 50-60% Higher				
<b>Capitalization</b>		<b>Base Case Price Target</b>		
	<b>FQ2A</b>	<b>F2021E</b>		
<b>Share Price as of 02/03/20</b>	<b>42.17</b>	<b>Revenue</b>	<b>EBITDA</b>	<b>Mult Valuation</b>
Diluted Shares	55	KFY Core	\$1,931 \$193	7.0x \$1,348
<b>Market Capitalization</b>	<b>2,307</b>	KFY RPO	252 43	14.0x 599
Plus: Total Debt	273	KFY Digital	424 121	12.0x 1,450
Add: Cash for Deferred Comp	263	Less: Net Debt <sup>(2)</sup>		(40)
Add: Cash for Recent M&A	113	Implied Market Capitalization		\$3,358
Less: Cash and equivalents	(609)	<b>Implied Share Price</b>		<b>\$61.36</b>
<b>Enterprise Value</b>	<b>2,347</b>	<b>Upside</b>		<b>45.5%</b>
Operating Leases	249	(2) Subtracts \$112.5m of FQ2A cash for Digital acquisitions		
Lease Adjusted EV	2,596			
<b>KFY Trading Statistics<sup>(1)</sup></b>		<b>Bull Case Price Target</b>		
	<b>FY 12/31</b>	<b>F2021E</b>		
	<b>F2019A F2020E F2021E</b>	<b>Revenue</b>	<b>EBITDA</b>	<b>Mult Valuation</b>
EV / Revenue	1.2x 1.2x 1.1x	KFY Core	\$205	8.0x \$1,640
EV / Adj. EBITDA	7.6x 7.7x 6.9x	KFY RPO	43	14.0x 599
EV / Adj. EBIT	11.6x 9.5x 8.1x	KFY Digital	121	12.0x 1,450
P / E	12.6x 13.5x 11.4x	Less: Net Debt <sup>(2)</sup>		(40)
EV / FCF	14.2x 16.0x 10.1x	Implied Market Capitalization		\$3,649
FCF / EV	7.0% 6.3% 9.9%	<b>Implied Share Price</b>		<b>\$66.69</b>
(1) Consensus estimates		<b>Upside</b>		<b>58.2%</b>
Source: Company filings, Kerrisdale analysis				

Korn Ferry offers durable growth at a discounted price. Over the past five years, revenue and earnings have doubled, the RPO has gone from a niche business to KFY's leading growth driver, and KFY Digital has emerged as a \$400m contributor that sets the business apart from its peers. With pockets of global uncertainty of late 2019 fading to the background – an initial trade war agreement was reached, the U.K. election concluded, and equity markets reached a new high -- investors will assess Korn Ferry for what it has become: a durable, digital-first service business.

## II. Company Overview

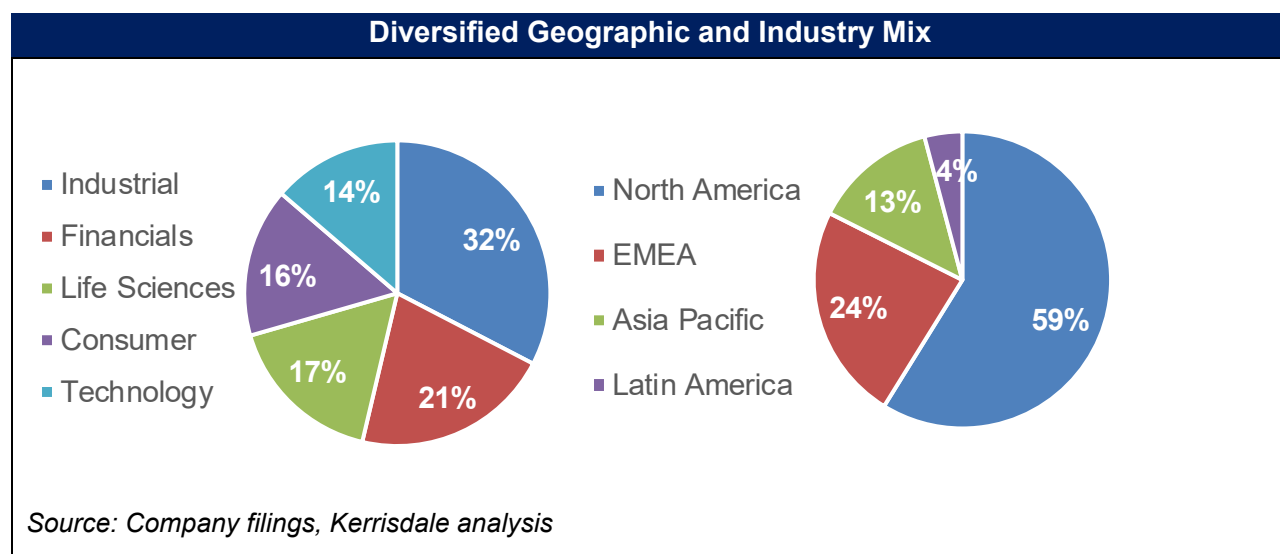
*“You’d think that the banker and lawyer are the first call when crisis strikes, but no, it’s the executive recruiter... because the recruiter can keep the secrets” – Industry executive*

Korn Ferry has been at the forefront of the executive staffing industry since its founding in 1969. As the [leader](#) of the “Big Five” (KFY, Spencer Stuart, Egon Zehnder, HSII, and Russell Reynolds), KFY’s search partners have placed industry titans throughout global industry – and, in many instances, placed these executives multiple times throughout their ascendant careers. As these relationships are cemented over the decades, Korn Ferry’s access to C-suites grows over time – it’s worked with 98% of the Fortune 100 and 93% of the FTSE 100, with 90% of engagements in F2019 on behalf of recurring clients. This unique platform within world

commerce gives KFY the ability to move into new business lines and monetize the extensive IP it has built over time, including 8m candidate profiles, 20m compensation datapoints, and 69m employee assessments. Management believes it can leverage the brand and relationships forged in Search to become a trusted supplier of digital platforms, RPO, and consulting services to executives everywhere.

Korn Ferry: Capitalization and Financial Results						
Capitalization			FY 17A	FY 18A	FY 19A	LTM
<b>Share Price as of 02/03/20</b>	<b>42.17</b>	<b>Revenue</b>				
Diluted Shares	55	Executive Search	623	618	709	765
<b>Market Capitalization</b>	<b>2,307</b>	Advisory	724	785	821	814
Plus: Total Debt	273	RPO + Prof Search	224	273	330	363
Add: Cash for Deferred Comp	263					
Add: Cash for Recent M&A	113	<b>EBITDA</b>				
Less: Cash and equivalents	(609)	Executive Search	137	159	194	191
<b>Enterprise Value</b>	<b>2,347</b>	Advisory	128	144	151	149
Operating Leases	249	RPO + Prof Search	33	43	54	61
Lease Adjusted EV	2,596	Corp Overhead	(63)	(67)	(88)	(87)

Source: Company filings, Kerrisdale analysis



Korn Ferry’s success has come from adding market share within a very fragmented end-market. The executive search landscape is primarily composed of sub-scale, niche private competitors. And yet KFY’s valuation is frequently compared against smaller search firms like Heidrick & Struggles or temp staffing firms like Robert Half. We think KFY’s insistence on avoiding temp work allows it to maintain brand equity and prestige: over 70% of its KFY Search assignments are for C-suite or senior executives, with exposure to all industries and geographies. In the prior fiscal year, KFY executed 6,800 assignments with 550 professionals, recognizing about \$1.4m of revenue per professional. These Search professionals are usually former industry executives with deep specialization and contracts in their respective fields.

## Human Resource Service Competitors

### DSP Human Capital Industry Taxonomy

Staffing	Executive Search	HR & Outsourcing Services	HR Technology
<p><b>United States</b>            AMN Healthcare (AMN)            Cross Country Healthcare (CCRN)            Kforce (KFRC)            Kelly Services (KELY.A)            Manpower Group (MAN)            On Assignment (ASGN)            Resources Connection (RECN)            Robert Half (RHI)            Trueblue (TBI)</p> <p><b>Europe</b>            Adecco (ADEN)            Brunel (BRNL:EN)            CRIT (CEN:EN)            Hays (LSE:HAS)            PageGroup (LSE:PAGE)            Randstad (ENXTAM:RAND)            Sthree (LSE:STHR)            Synergie (SDG:PA)</p> <p><b>Japan</b>            Recruit Holdings (TSE: 6098)            Persol Holdings (TSE: 2181)</p> <p><b>Select RPOs</b>            Accolo            ADP RPO            Advanced RPO            Advantage XPO            AgilOne            Alegis Global            Alexander Mann            Cielo            Engage2Excel            Hire Velocity            Hudson Global            Kinetix            Korn Ferry (FKA            Future5Step)            Method3            Newton Talent</p> <p>Novo Group            NXTThing RPO            Orion Novotus            PeopleScout (Trueblue)            Pontoon (Adecco)            PrincetonOne            Sevenstep (Motion            Recruitment Partners)            Sourceright (Randstad)            TalentRISE            Taylor Strategy Partners            TruStar Talent Solutions            WilsonHCG            Xelerate            Yoh RPO</p> <p><small>DELANCEY STREET PARTNERS, LLC</small></p>	<p>Heidrick and Struggles (HSII)            Korn Ferry International (KFY)</p> <p><b>Select Private Executive Search</b>            Boyden            Caldwell Partners            DHR International            Egon Zehnder            LLC Partners            N2Growth            Odger Berndtson            On Partners            Russell Reynolds            Signium            Spencer Stuart            Stanton Chase International            Transearch            True Search            Witt/Kieffer</p>	<p>Automatic Data Processing (ADP)            Barrett Business Services (BBSI)            Capita (LSE:CPI)            Insperity (NSP)            Paychex (PAYX)            Towers Watson (TW)            TriNet Group (TNET)            WageWorks (WAGE)</p> <p><b>New World Staffing, Gig and Community</b>            Fiverr            Freelancer.com            GLG            MBO Partners            Patina Solutions            Snagajob            TaskRabbit            TopTal            Uber Works            Upwork            WeWork            Wonolo</p>	<p><b>Enterprise/Core HRIS</b>            Oracle Corporation (ORCL)            SAP SE (DB:SAP)            Workday, Inc. (WDAY)            Sage Group plc (LSE:SGE)</p> <p><b>Social/Community</b>            Facebook (FB)            XING AG (XTRA:01BC)</p> <p><b>Payroll/Benefits Technology</b>            Benefit Focus (BNFT)            Intuit (INTU)            Ultimate Software (ULTI)            Paylocity (PCTY)            Paycom (PAYC)            Ebix (EBIX)            eHealth (EHTH)            Health Equity (HQQ)</p> <p><b>Administrative Technology</b>            Azure Software (ASUR)            Zendesk (NYSE: ZEN)</p> <p><b>Learning/Performance/Assess</b>            Cornerstone OnDemand (CSOD)            Healthstream (HSTM)</p> <p><b>Recruitment Technology</b>            SEEK (ASX:SEEK)            51job (JOBS)            Dice Holdings (DHX)</p>

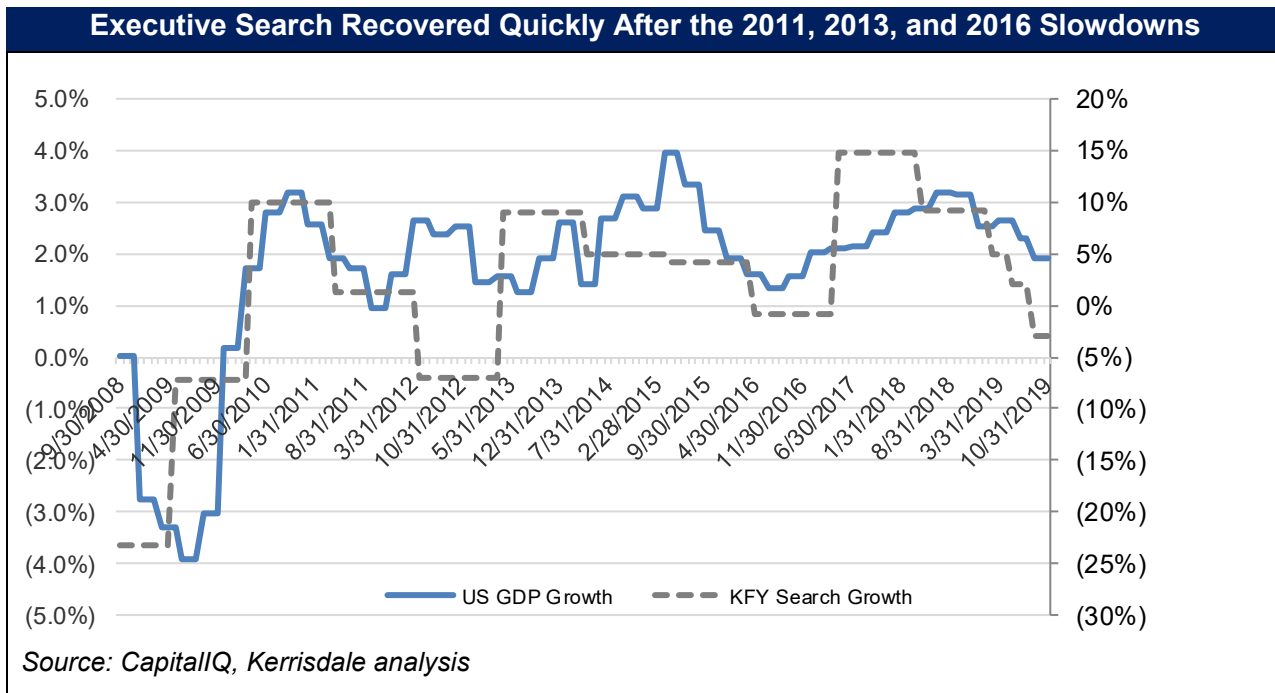
Source: S&P Capital IQ

HCM: STAFFING, RPO & EXECUTIVE SEARCH UPDATE

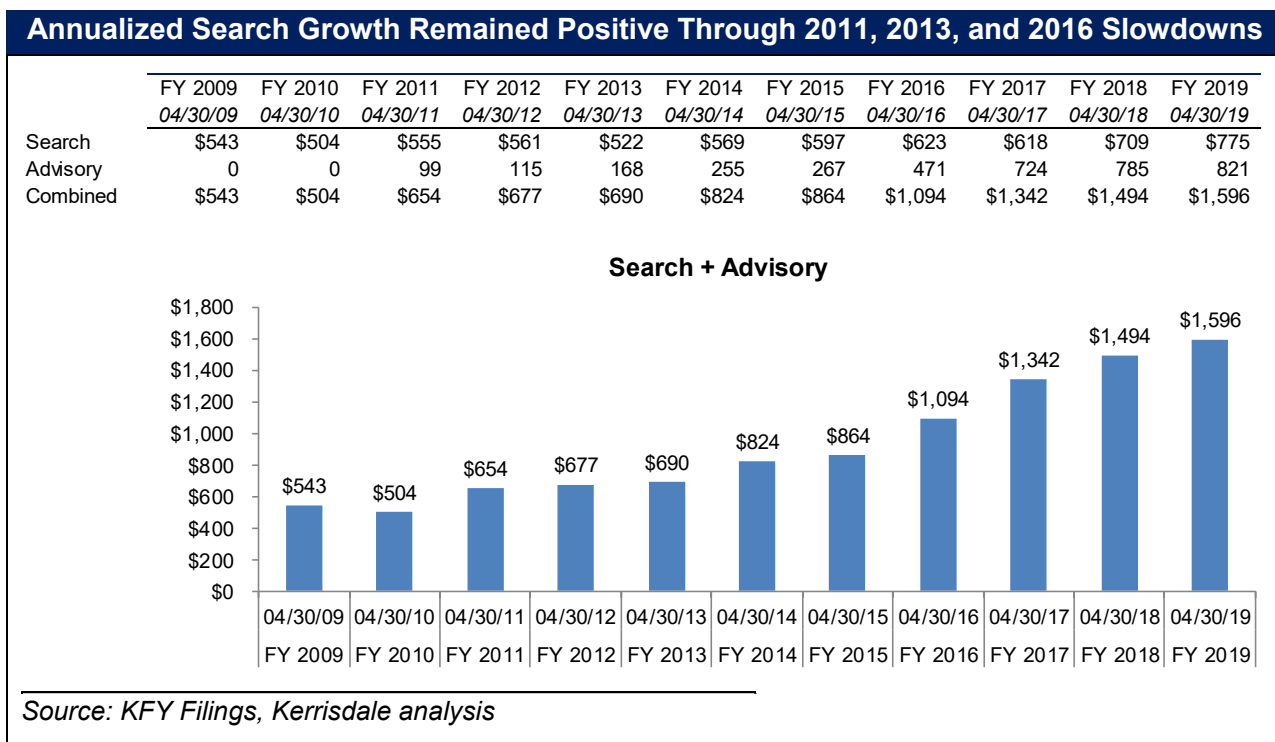
Source: Delancey Street December 2018 Human Capital Report

With the 2009 credit crisis still lingering on market psyche, any cyclical slowdown is brandished as reason to sell the staffing names, explaining Korn Ferry’s remarkably cheap valuation multiples amidst a market still near all-time highs. While the Search business does pause for a quarter or two during periods of business uncertainty – KFY saw this occur during the 2011, 2013, and 2016 periods – growth is quick to return as economic conditions improve.

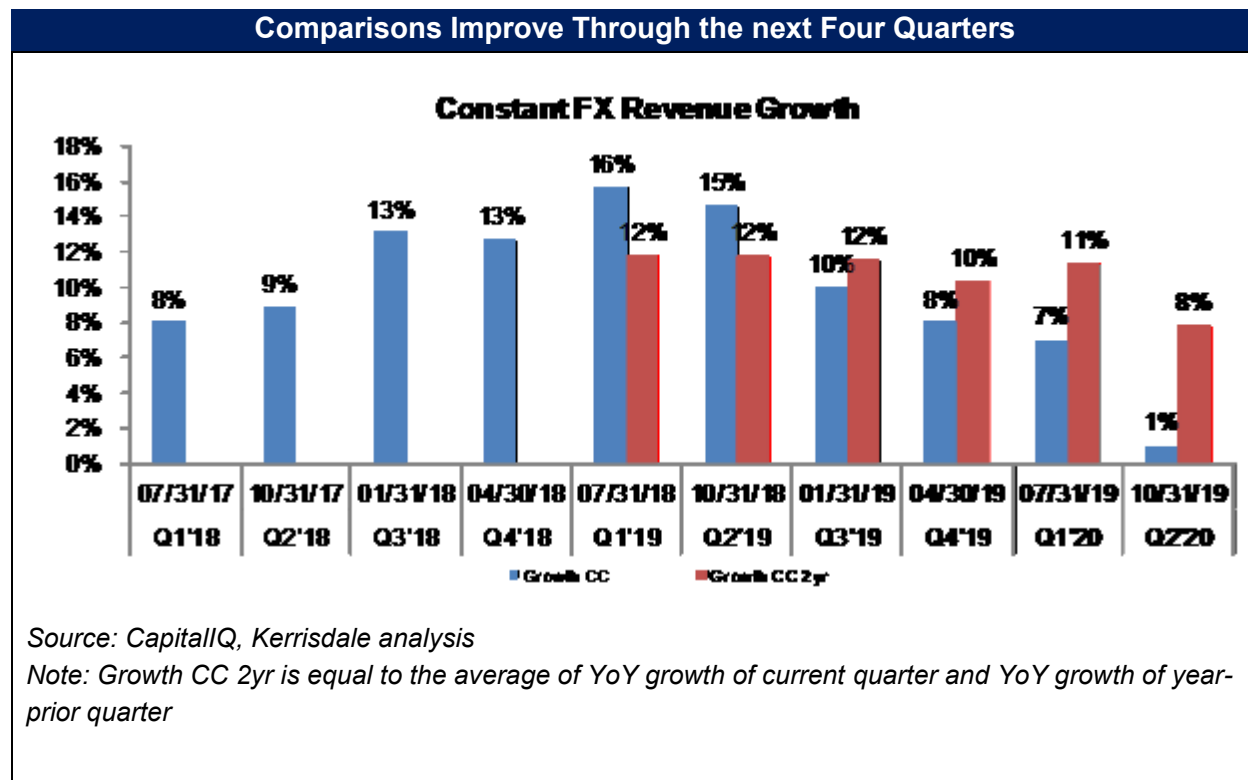




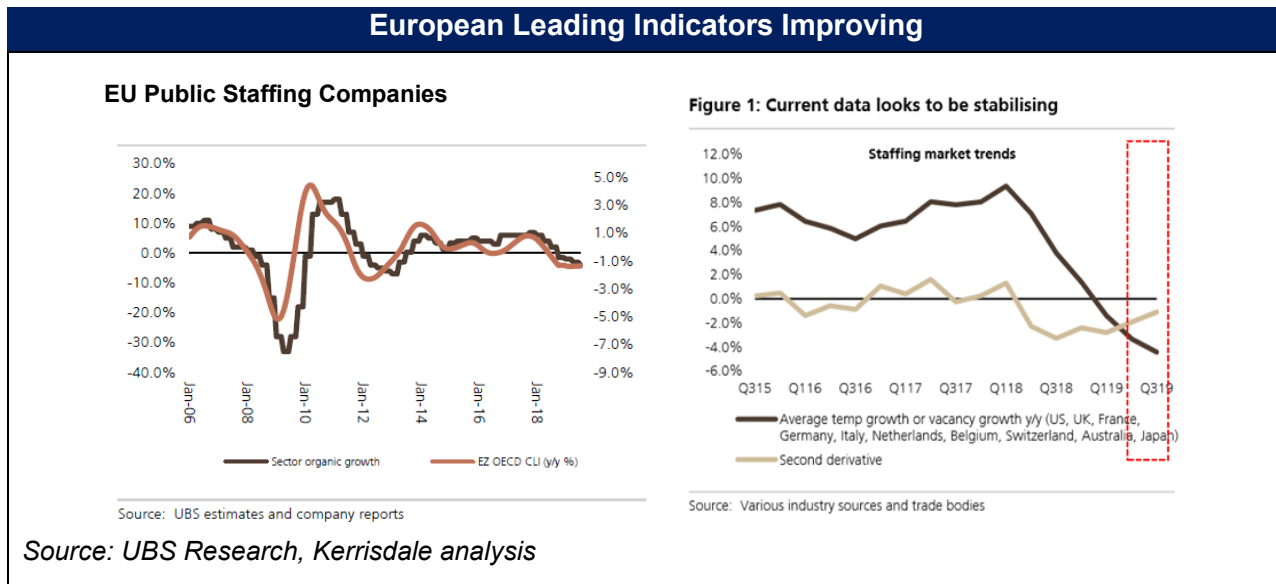
Korn Ferry’s clean balance sheet affords it strategic flexibility during these cyclical downturns. The 2015 acquisition of Hay Group bolstered Advisory revenue the following year. We think the November 2019 acquisition of Miller Heiman, AchieveForum, and Strategy Execution follows a similar pattern: adding \$120m+ of high-margin revenue during a period of short-term stress.



The recovery in Search and Advisory will be aided by easier comparisons in the coming fiscal year. Measured on a two-year basis and adjusted for FX, KFY's constant currency growth remained stable at +8% in FQ2. As KFY laps the double-digit growth figures from 2018, and with a more favorable FX backdrop, growth should accelerate in F2021.



Analysts from leading banks are already pointing to an improvement in business sentiment. The OECD's (Organisation for Economic Co-operation and Development) composite of leading indicators bottomed in Q3/Q4 2019 – any sign of an improvement directly benefits Korn Ferry's European business (24% of search revenue).



But even without help from the European environment, we see KFY shares outperforming as it introduces Wall Street to its digital business.

### III. Newly Disclosed Korn Ferry Digital Business to Unlock Value

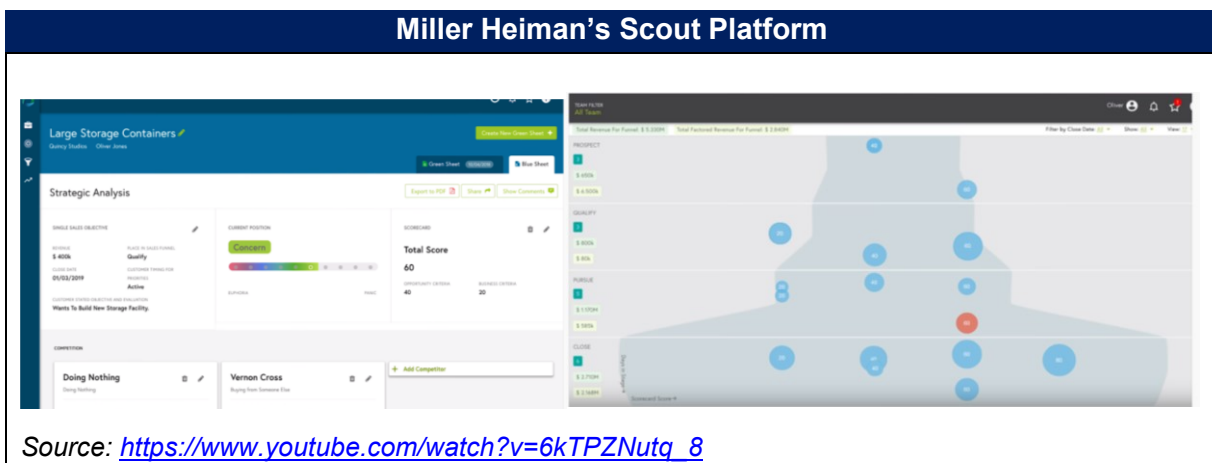
For the first time in the F2019 10-K, Korn Ferry disclosed a revenue figure for its proprietary digital products, hidden deep within its financial filings. The market appears to have ignored this disclosure for now, but that should change after KFY breaks Digital out into an independent reporting segment in its upcoming quarterly press release. While the core staffing business exhibits business cyclical – hiring grows over time but pauses during periods of uncertainty – KFY’s Digital business can hold firm during periods of stress. Customers are loathe to cancel licenses for daily-use tools like compensation databases and talent assessment files. Newer products like software and training for sales representatives become profit-centers as they drive improved sales productivity. As uptake grows for these data-driven tools, KFY’s margins benefit from lower incremental costs: unlike KFY’s people-driven Search and Consulting practices, each new Digital revenue dollar requires little new operating expense.

Digital Products (as of F2019 10-K)				
Advisory	FY 2017	FY 2018	FY 2019	% Total
Consulting	497.7	540.5	568.3	69%
Growth	--	8.6%	5.1%	
Products	226.6	244.5	252.7	31%
Growth	--	7.9%	3.4%	

*Source: Korn Ferry F2019 10-K*

As of the F2019 10-K, Digital products contributed over \$250m in revenue. But this figure will jump to \$400m, or 20% of overall fee revenue, after the November [acquisition](#) of three new digital training tools (\$125m of acquired revenue). The new portfolio consists of \$100m of revenue from rewards databases, \$120m for assessment & succession, \$120m in learning development/sales training, and \$60m for organizational strategy. Korn Ferry’s compensation [database](#) is a world-leader, with 20 million high-quality records for base salaries, incentive structures, and benefits programs. Its leadership assessment [tools](#) were built over 50 years, amassing 70 million leadership profiles used to assess employee skill-matching. This Big Data approach separates KFY Digital from competitors, with customers frequently remarking on the robustness of these solutions.

The largest of KFY’s recently acquired tools is the Miller Heiman sales productivity [portfolio](#) (about \$90m in revenue), a collection of training and software tools well-liked by enterprise and mid-market sales departments (4.1 Rating out of 5.0 on G2.com) for its robust approach to monitoring, tracking, and closing deals. Miller Heiman’s recently introduced “Scout” product adds a software tool to assimilate these tactics into a CRM-like sales tracking funnel.



The trio of assets acquired in November was run by TwentyEighty, a private equity spinoff that suffered from too much debt and a lack of investment. By acquiring these assets under Korn Ferry’s existing infrastructure and by leveraging its enviable list of global blue-chip clients, KFY can quickly drive improved EBITDA margins while cross-selling its new suite of digital tools. A shared services agreement signed between KFY and TwentyEighty expiring in FQ4 forces duplicative costs through April 2020, but as this agreement lapses and severance costs taper, KFY can quickly increase EBITDA margins to 27-30% by the beginning of F2021. With \$125m of acquired revenue, these deals plus internal restructuring efforts add \$35-40m to F2021 EBITDA, or \$0.40 - \$0.45c of EPS – accretion the market may have overlooked since KFY’s current guidance for FQ3 includes the duplicative costs of the shared service agreement. This near-term accretion opportunity will further come to light as Korn Ferry breaks out its newly enlarged Digital business in the upcoming fiscal third quarter.

Current consensus models assume KFY's core Search and Advisory are flat-to-down over the next six quarters – a premature assumption since KFY only guides one quarter in advance. KFY's operating history has shown that pauses generally only last a few quarters, making it unlikely that Search and Advisory earnings decline again throughout F2021. But even with these conservative assumptions, the addition of the acquired businesses adds around \$40m of EBITDA to the pro-forma business. With that accretion alone, KFY will go from a no-growth business in F2020, to one growing EBITDA by 10-15%+ in F2021. As this earnings inflection occurs, it's unlikely that KFY continues to trade at a paltry 7x EBITDA.

<b>Acquisitions to Add \$35-40m of EBITDA in F2021</b>						
					<b>GS</b>	<b>ProFrm</b>
<b>Revenue</b>	<b>F2017</b>	<b>F2018</b>	<b>F2019</b>	<b>LTM</b>	<b>F2020E</b>	<b>F2021E</b>
Executive Search	618	709	775	765	733	770
KF Consulting	498	541	568	539	518	544
KF Digital	227	245	253	275	275	424
<i>Memo: November Acquisitions (\$125m FY, closed Nov 2019)</i>					83	
Total Advisory	724	785	821	814	876	968
Pure-RPO	--	--	175	192	210	252
Professional Services	--	--	155	171	175	193
Total RPO	224	273	330	363	385	444
<b>Fee Revenue</b>	<b>1,566</b>	<b>1,767</b>	<b>1,926</b>	<b>1,942</b>	<b>1,995</b>	<b>2,182</b>
<b>EBITDA</b>						
Executive Search	137	159	194	191	177	185
KF Consulting	--	--	--	--	67	71
KF Digital	--	--	--	--	84	121
Total Advisory	128	144	151	149	151	192
Pure-RPO	--	--	--	--	36	43
Professional Services	--	--	--	--	30	31
Total RPO	33	43	54	61	66	74
Corporate Overhead	(63)	(67)	(88)	(87)	(88)	(94)
<b>EBITDA</b>	<b>235</b>	<b>278</b>	<b>311</b>	<b>313</b>	<b>305</b>	<b>356</b>
<b>Y/Y Growth</b>					(3%)	17%

*Source: KFY Filings, Goldman Sachs Research, Kerrisdale analysis*

Owing to the recurring nature of its product suite, high incremental margins, and ability to generate consistent growth, we think Korn Ferry's Digital business is worth at least 12x EBITDA. Standalone consulting firms with digital consulting practices trade for 12-15x+ forward EBITDA, even with low-single-digit growth estimates for the full year. FTI Consulting (FCN), a corporate restructuring and legal consultancy, trades for 13x 2020E EBITDA; ICF International (ICFI), a government policy and digital consulting firm, also trades for 13x 2020E EBITDA, and Huron Consulting (HURN), a healthcare and education consulting group, trades for almost 15x 2020E EBITDA. As KF Digital proves itself to be more like a corporate consultant and software business, and less like a staffing company, it could even justify a multiple in excess of our 12x EBITDA estimate.

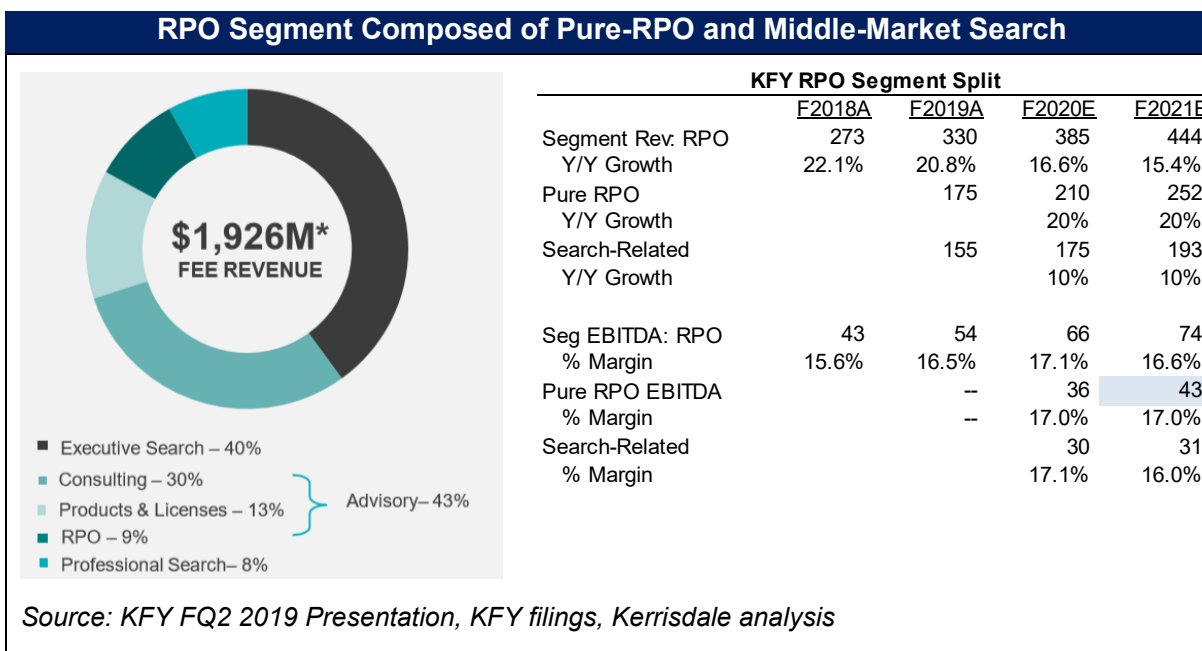
Digital Consulting Assets Trade for 12-15x EBITDA						
Ticker	Company	EV / EBITDA		P / E		Rev Growth
		2020E	2021E	2020E	2021E	2020E
<b>Digital Comparables</b>						
FCN	FTI Consulting	13.1x	12.5x	21.1x	19.8x	5.4%
ICFI	ICF International	12.8x	12.0x	19.4x	16.8x	10.2%
HURN	Huron Consulting	14.9x	12.6x	23.1x	17.8x	6.3%
<b>Average</b>		<b>13.6x</b>	<b>12.4x</b>	<b>21.2x</b>	<b>18.2x</b>	

*Note: All operate on calendar fiscal years*  
*Source: CapitalIQ*

Even putting aside our standalone valuation arguments, the inclusion of Miller Heiman, Strategy Execution, and AchieveForum add 10-15%+ to underlying EBITDA and EPS growth beginning this April. The inevitable growth of the Digital businesses should be nicely complemented by KFY's second oft-forgotten asset: a recruiting process outsourcing business growing contracted revenue at 20%+/year since 2014.

## IV. Korn Ferry's Contracted RPO Business Worth 14x EV/EBITDA

Korn Ferry's RPO business has quietly compounded at 20% since F2015 with little variability and consistent new business wins. Even during 2016 when Search reported flat or slightly negative quarters, the as-disclosed RPO segment – current disclosures lump contracted RPO with a more variable middle-market Professional Search services – grew 9-13% through the same quarters. If we assume a roughly equal mix, as confirmed in the FQ1 2020 investor presentation (53% pure-RPO/47% Professional Search), the pure-RPO segment probably grew 20% even in 2016. This product began as a niche business to supplement executive recruiting but has now become 10% of KFY's revenue – certainly worth investors' attention. Assuming its growth continues, it should reach \$40-45m of EBITDA contribution next fiscal year, or about 13% of current consensus.



Management is taking steps to highlight the recurring nature of its pure-RPO segment. After providing the mix breakdown at the end of last year, it's spent time on quarterly calls highlighting the segment's new business wins. The most recent quarter marked a seasonal record for new wins at \$118m of long-term RPO contracts. These are typically 3-5-year contracts with retainer fees and recurring variable hiring requirements – minimum hiring goals are frequently given over the contracted timeframe – providing KFY with much higher visibility than a typical staffing assignment. As outsourcing contracts mature into their third and fourth years, companies find themselves ever more reliant on their RPO provider, aiding the renewal process. Of the \$118m in new wins, more than half came from existing clients.

Quarterly Contract Wins for RPO at Seasonal Records							
	Q4'18	Q1'19	Q2'19	Q3'19	Q4'19	Q1'20	Q2'20
	04/30/18	07/31/18	10/31/18	01/31/19	04/30/19	07/31/19	10/31/19
<b>RPO New Business</b>	<b>158</b>	<b>70</b>	<b>73</b>	<b>104</b>	<b>84</b>	<b>97</b>	<b>150</b>
Professional Search	38	31	32	26	34	31	32
<b>Long-term RPO contracts</b>	<b>120</b>	<b>39</b>	<b>41</b>	<b>78</b>	<b>50</b>	<b>66</b>	<b>118</b>
Of which: new logos				19	44	32	49
Of which: extensions				59	6	34	69

*Source: KFY Quarterly Calls*

RPO contracts are also an important component of KFY's expansion into Marquee and Regional accounts (now 30% of revenue, with a target of 40-45%), as leading clients hire Search for executive recruiting assignments, KF Digital for compensation and training programs, and the RPO for a 100-person regional staffing need. These larger enterprises are also more likely to invest during periods of economic contraction, fortifying the business as it builds a full product suite to serve the needs of corporations like Mars, CDK Global, and Expedia.

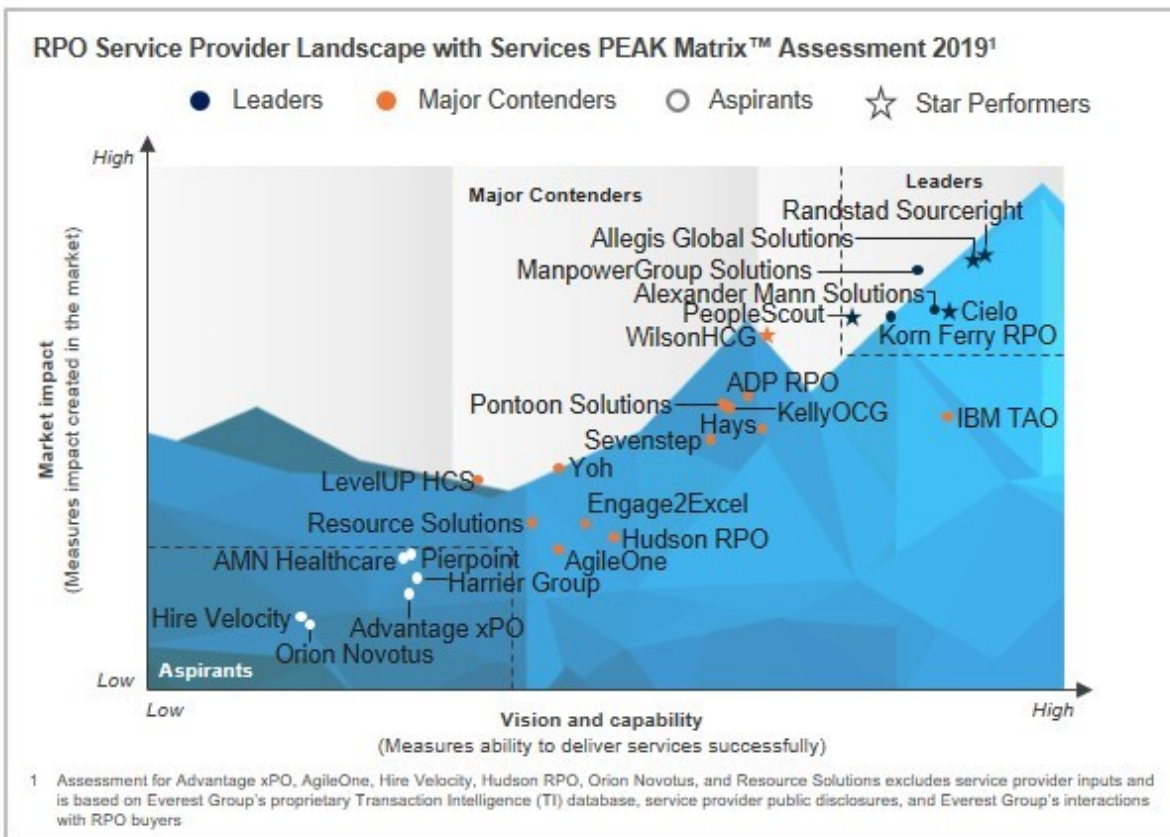
Examples of RPO assignments include hiring, onboarding, and retaining 15 database engineers housed in Eastern Europe, backfilling 50 sales-managers for a global pharma company, or even churn-management for a 1,000-employee pool of local store managers. Core functions like background checks, skill assessments, and screening are entirely outsourced to the RPO. Project sizes can vary from several hundred thousand dollars to, more specifically, one assignment KFY signed in F2018 worth \$60m over 5 years.



According to research provider Everest Group’s 2019 RPO [report](#), “The global RPO market witnessed a tremendous growth in 2018 as the market witnessed a significant uptick in activity across buyer segments, industries and geographies.” Several privately-owned companies like Cielo, Allegis, and Alexander Mann rank near the top of the category – the lack of an RPO-focused public comparable may explain the market’s decision to overlook KFY’s RPO for so long. Korn Ferry’s RPO ranks in the upper-right quadrant alongside these private companies and the large European staffing names, impressive given KFY’s market capitalization is less than half of Manpower’s and a fourth of Randstad’s.



KFY RPO Ranked as a Top-Tier Provider



Source: Everest Group

Owing to its embedded high-growth, recurring revenue model, and longer-dated contracts, RPOs can trade for mid-teens multiples of EBITDA and above. SunTrust believes KFY's RPO is worth 15x EV/EBITDA, supported by a median multiple of 14x for precedent transactions since 2015. Recent high-profile private equity [acquisitions](#) of Alexander Mann (\$1.1bn) and Cielo reveal an active market for RPO assets. We think KFY's RPO is worth 14x EV/EBITDA, and perhaps more owing to its exposure to a top-tier client list and a premium brand name. While we wouldn't expect KFY to carve off the asset, a private equity buyer could assess the RPO valuation in the context of a full takeout. If the market refuses to put a proper valuation on KFY shares, a private buyer eventually might.

## V. Valuation and Conclusion

Korn Ferry's valuation benefits from a very low starting point: it maddeningly trades at a discount not only to more cyclical peers like Robert Half (RHI), but also to slower-growth European-centric firms like Randstad and Manpower. Temp-staffing firm Robert Half trades for

10x C2020E EV/EBITDA with the European-centric names at 8-9x EBITDA, all well ahead of KFY's cut-rate 7x EV/EBITDA. This can't be explained by growth expectations: the fresh Digital units and easy comparisons for Search give rise to KFY's double-digit earnings growth estimates; comparable peers are expected to achieve less than half of that.

KFY Shares Trade at 2x Discount to Global Staffing Peer Group							
Ticker	Company	EV / EBITDA		P / E		EPS Growth	
		2020E	2021E	2020E	2021E	2020E	2021E
<b>Executive Recruiting</b>							
RHI	Robert Half	9.3x	8.9x	14.1x	13.3x	6.4%	5.6%
ADEN	Adecco Group	8.8x	8.3x	12.3x	11.7x	0.6%	5.0%
RAND	Randstad	8.0x	7.7x	12.4x	11.7x	1.3%	5.1%
MAN	ManpowerGroup	7.7x	7.1x	12.1x	11.2x	3.3%	7.8%
<b>Average</b>		<b>8.4x</b>	<b>8.0x</b>	<b>12.7x</b>	<b>12.0x</b>		
KFY	Korn Ferry	7.0x	6.4x	12.0x	10.2x	10.6%	16.7%
<i>Note: Consensus estimates adjusted to a Dec 31st calendar year</i>							
<i>Source: CapitalIQ</i>							

And KFY's earnings are tangible: recurring capital requirements are low while full year working capital needs are balanced, leading to high free cash flow conversion. KFY even expenses share-based compensation (about \$0.40/share), an increasingly rare and conservative reporting standard in a market usually willing to overlook its cost. Given KFY's reliable FCF in recent years, which will improve as the business mix shifts towards high-margin Digital services, we've also valued shares with a long-term DCF model. With still-conservative inputs like an 8% discount rate, a 14x terminal FCF multiple, and modeled global slowdowns, we believe shares can trade for \$80, a 90% premium to the current valuation.

## Steady FCF Generation Suggests 90% DCF Upside

	Historical					Projected									
	F2015A	F2016A	F2017A	F2018A	F2019A	F2020E	F2021E	F2022E	F2023E	F2024E	F2025E	F2026E	F2027E	F2028E	F2029E
Search	597	623	618	709	775	733	770	832	782	829	911	921	884	893	928
Growth	5.0%	4.3%	(0.8%)	14.8%	9.3%	(5.4%)	5.0%	8.0%	(6.0%)	6.0%	10.0%	1.0%	(4.0%)	1.0%	4.0%
Digital & Advisory	267	471	724	785	821	876	968	1,045	1,024	1,127	1,240	1,302	1,276	1,339	1,406
Growth	4.9%	76.4%	53.7%	8.4%	4.6%	6.7%	10.4%	8.0%	(2.0%)	10.0%	10.0%	5.0%	(2.0%)	5.0%	5.0%
RPO	164	198	224	273	330	385	444	516	598	694	805	917	1,028	1,151	1,266
Growth	19.7%	21.0%	12.9%	22.1%	20.8%	16.6%	15.4%	16.0%	16.0%	16.0%	16.0%	14.0%	12.0%	12.0%	10.0%
<b>Total Revenue</b>	<b>1,028</b>	<b>1,292</b>	<b>1,566</b>	<b>1,767</b>	<b>1,926</b>	<b>1,995</b>	<b>2,182</b>	<b>2,393</b>	<b>2,404</b>	<b>2,649</b>	<b>2,956</b>	<b>3,140</b>	<b>3,187</b>	<b>3,383</b>	<b>3,600</b>
Growth		25.7%	21.2%	12.9%	9.0%	3.6%	9.4%	9.6%	0.5%	10.2%	11.6%	6.2%	1.5%	6.1%	6.4%
EBITDA Margin: Search	22.2%	24.4%	22.2%	22.5%	25.0%										
EBITDA Margin: Advisory	16.6%	16.7%	17.7%	18.3%	18.4%										
EBITDA Margin: RPO	14.1%	14.9%	14.7%	15.6%	16.5%										
	← Modeled Global Slowdowns →														
Compensation & Benefits	(691)	(897)	(1,072)	(1,199)	(1,311)	(1,360)	(1,475)	(1,603)	(1,659)	(1,801)	(1,980)	(2,119)	(2,199)	(2,300)	(2,412)
% of Revenue	67.3%	69.5%	68.4%	67.9%	68.1%	68.2%	67.6%	67.0%	69.0%	68.0%	67.0%	67.5%	69.0%	68.0%	67.0%
Cost of Service	(40)	(60)	(71)	(74)	(75)	(78)	(86)	(94)	(94)	(104)	(116)	(123)	(125)	(133)	(141)
Gross Profit	\$297	\$335	\$423	\$494	\$539	\$556	\$622	\$696	\$651	\$744	\$860	\$897	\$863	\$950	\$1,047
G&A	(146)	(213)	(226)	(237)	(245)	(253)	(268)	(294)	(313)	(318)	(355)	(377)	(382)	(406)	(432)
% of Revenue	14.2%	16.5%	14.5%	13.4%	12.7%	12.7%	12.3%	12.3%	13.0%	12.0%	12.0%	12.0%	12.0%	12.0%	12.0%
EBITDA	\$151	\$122	\$196	\$257	\$294										
Other Income and Addbacks	8	68	39	21	17	3	3	3	3	3	3	3	3	3	3
<b>Adj EBITDA</b>	<b>\$159</b>	<b>\$189</b>	<b>\$235</b>	<b>\$278</b>	<b>\$311</b>	<b>\$305</b>	<b>\$356</b>	<b>\$404</b>	<b>\$341</b>	<b>\$429</b>	<b>\$507</b>	<b>\$523</b>	<b>\$483</b>	<b>\$547</b>	<b>\$618</b>
Margin	15.5%	14.7%	15.0%	15.7%	16.1%	15.3%	16.3%	16.9%	14.2%	16.2%	17.2%	16.7%	15.2%	16.2%	17.2%
D&A	(28)	(36)	(47)	(49)	(46)	(48)	(52)	(57)	(58)	(64)	(71)	(75)	(76)	(81)	(86)
% of Revenue	2.7%	2.8%	3.0%	2.7%	2.4%	2.4%	2.4%	2.4%	2.4%	2.4%	2.4%	2.4%	2.4%	2.4%	2.4%
Adj EBIT	132	153	188	229	264	258	303	347	283	365	437	448	407	465	531
Margin	12.8%	11.9%	12.0%	13.0%	13.7%	12.9%	13.9%	14.5%	11.8%	13.8%	14.8%	14.3%	12.8%	13.8%	14.8%
<b>Free Cash Flow</b>															
NOPAT (22% taxes)						201	237	270	221	285	340	349	317	363	414
Plus: D&A						48	52	57	58	64	71	75	76	81	86
Less: Capex	(22)	(26)	(50)	(42)	(47)	(162)	(57)	(62)	(63)	(69)	(77)	(82)	(83)	(88)	(94)
% of revenue	2.1%	2.0%	3.2%	2.4%	2.4%	2.5%	2.6%	2.6%	2.6%	2.6%	2.6%	2.6%	2.6%	2.6%	2.6%
<b>Free Cash Flow</b>						<b>86</b>	<b>232</b>	<b>266</b>	<b>216</b>	<b>279</b>	<b>335</b>	<b>343</b>	<b>311</b>	<b>356</b>	<b>407</b>
<b>Discounted Value of Interim Cash Flows</b>						<b>83</b>	<b>207</b>	<b>219</b>	<b>165</b>	<b>198</b>	<b>219</b>	<b>208</b>	<b>175</b>	<b>185</b>	<b>196</b>
Discount Rate	8.0%														
Terminal FCF Multiple	14.0x														
Terminal Value	5,700														
Discounted Interim CFs	1,855														
Discounted Terminal Value	2,744														
<b>Total Enterprise Value</b>	<b>\$4,598</b>														
Less: Debt	(649)														
Plus: Cash	609														
<b>Total Equity Value</b>	<b>\$4,559</b>														
Implied Share Price	<b>\$80.49</b>														
Upside	91%														

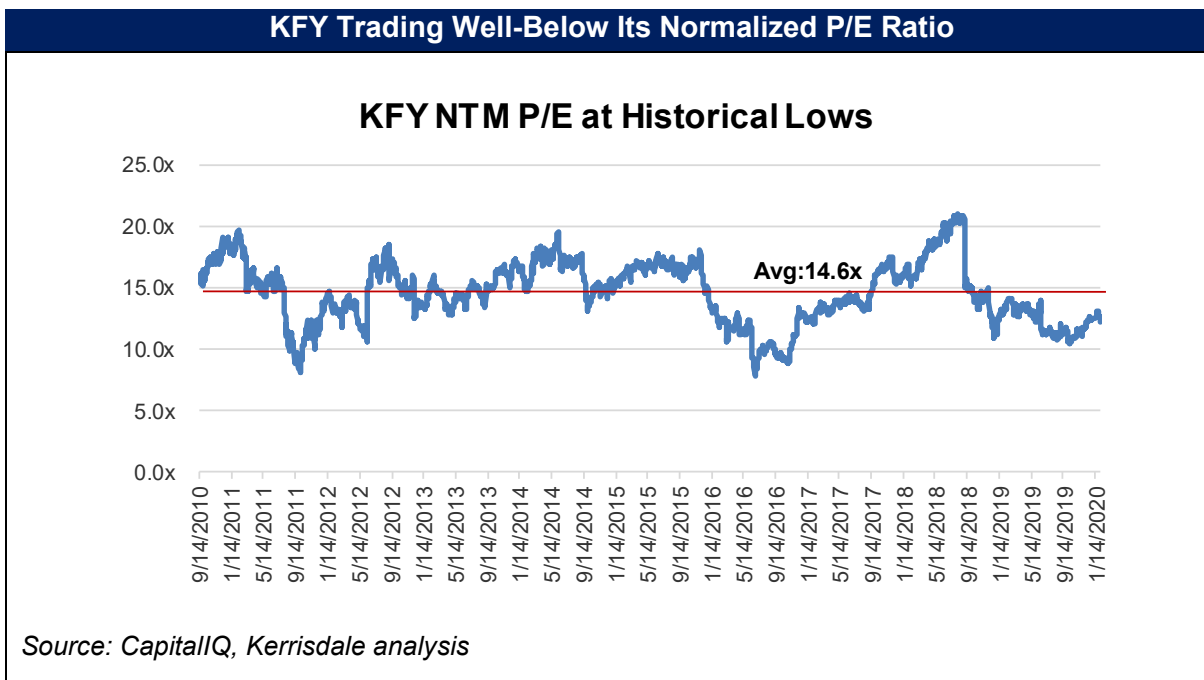
Source: KFY Filings, Kerrisdale analysis

And this substantial fundamental upside is paired with an imminent revaluation catalyst: next quarter's new Digital disclosures and the 10-15% accretion expected by the April 2020 quarter. At the start of F2021 KF Digital becomes a \$400m revenue business with an EBITDA contribution of over \$100m (targeted margins of 27-30%). The RPO segment, in turn, will grow into a \$75m EBITDA business, of which \$40m is contracted RPO (i.e. 3-5 year assignments with recurring projects) and \$35m is middle-market professional search. With the overall company projected to post \$310m of consolidated EBITDA in F2020, Digital and contracted RPO together become substantial contributors and should elevate KFY's valuation ahead of traditional staffing firms.

And in assessing the core Search business, investors should review the cyclical slowdowns in 2011, 2013, and 2016: Search did decline for a few quarters in each instance, but KFY's business was quick to recover as economic turbulence receded. This time, KFY's trio of training tools acquired in November 2019 add \$35-40m to KFY's EBITDA and \$0.40-0.45 to EPS, creating a springboard for growth into F2021. Growing business like this don't trade for 11x earnings, especially ones with a high-margin digital leadership presence.

Valuation and Price Target						
<b>Capitalization</b>		<b>Base Case Price Target</b>				
	<b>FQ2A</b>	<b>F2021E</b>				
<b>Share Price as of 02/03/20</b>	<b>42.17</b>	<u>Revenue</u>	<u>EBITDA</u>	<u>Mult</u> <u>Valuation</u>		
Diluted Shares	55	KFY Core	\$1,931	\$193	7.0x	\$1,348
<b>Market Capitalization</b>	<b>2,307</b>	KFY RPO	252	43	14.0x	599
Plus: Total Debt	273	KFY Digital	424	121	12.0x	1,450
Add: Cash for Deferred Comp	263	Less: Net Debt <sup>(2)</sup>				(40)
Add: Cash for Recent M&A	113	Implied Market Capitalization				\$3,358
Less: Cash and equivalents	(609)	<b>Implied Share Price</b>				<b>\$61.36</b>
<b>Enterprise Value</b>	<b>2,347</b>	<b>Upside</b>				<b>45.5%</b>
Operating Leases	249	(2) Subtracts \$112.5m of FQ2A cash for Digital acquisitions				
Lease Adjusted EV	2,596					
<b>KFY Trading Statistics<sup>(1)</sup></b>		<b>Bull Case Price Target</b>				
	<b>FY 12/31</b>	<b>F2021E</b>				
	<u>F2019A</u> <u>F2020E</u> <u>F2021E</u>	<u>Revenue</u>	<u>EBITDA</u>	<u>Mult</u> <u>Valuation</u>		
EV / Revenue	1.2x 1.2x 1.1x	KFY Core	\$205	8.0x	\$1,640	
EV / Adj. EBITDA	7.6x 7.7x 6.9x	KFY RPO	43	14.0x	599	
EV / Adj. EBIT	11.6x 9.5x 8.1x	KFY Digital	121	12.0x	1,450	
P / E	12.6x 13.5x 11.4x	Less: Net Debt <sup>(2)</sup>			(40)	
EV / FCF	14.2x 16.0x 10.1x	Implied Market Capitalization			\$3,649	
FCF / EV	7.0% 6.3% 9.9%	<b>Implied Share Price</b>			<b>\$66.69</b>	
(1)Consensus estimates		<b>Upside</b>			<b>58.2%</b>	
<i>Source: Kerrisdale analysis, CapitalIQ, Company filings</i>						

As the strength of KFY's business units comes to light, we believe shares can trade towards \$60-65, more than 50% higher. The digital business can trade closer to digital consulting peers like HURN and FCN, the contracted RPO can earn a growth multiple, and improved results for core Search and consulting can push KFY off of its trough multiple. At a share price of \$65, KFY would trade at just 17x P/E – more consistent with its valuation over time.



In a market reaching daily highs every day, shares of Korn Ferry offer a unique opportunity: a cheap valuation with a clean balance sheet, new disclosures that re-categorize KFY from a niche staffing firm to a digital-led services business, and an expected 10-15% of EPS accretion after acquired products roll off their shared services agreement. A 50-year history has created a treasure trove of data: a compensation database with 20 million real-world precedents, leadership assessment tools incorporate 70 million prior assessments, and leading sales training toolkits and software. Above-market growth should return in the April 2020 fiscal year as KFY laps much easier comparisons and its contracted RPO and Digital products become a greater portion of mix. Say goodbye to the overlooked, under-covered KFY and say hello to the new Korn Ferry Digital.

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